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Hong Kong Tax Newsflash: Hong Kong removed from EU watchlist on tax cooperation

On 12 March 2019, the European Commission announced updates to the EU list of non-cooperative tax jurisdictions. Hong Kong has been removed from EU's watchlist on tax cooperation.

Background

The EU list of non-cooperative jurisdictions was initially released in December 2017 as part of the EU's initiative to tackle tax avoidance and evasion and promote fairer taxation within the EU and globally. The list, which has been revised several times, originally cited 17 jurisdictions as failing to meet good governance tax standards ("blacklist jurisdictions"), and 47 jurisdictions, including Hong Kong, that committed to address deficiencies in their tax systems and meet the required criteria were included on a "watchlist". Hong Kong was required to endeavour to meet the relevant EU criteria by the end of 2018 to avoid being moved from the watch list to the blacklist.

EU tax cooperation criteria

The EU set out three good tax governance criteria:

Transparency: The jurisdiction must comply with international standards on the automatic exchange of information and information exchange (AEOI) on request.

Fair tax competition: The jurisdiction must not have any harmful tax regimes that are not in line with the principles of the EU Code of Conduct or the OECD Forum on Harmful Tax Practices.

Base Erosion Profit Shifting (BEPS): The jurisdiction must commit to implementing the four minimum standards under the OECD BEPS project.

Hong Kong's actions to meet the criteria

In 2016, Hong Kong indicated to the OECD that it was committed to the implementation of the BEPS minimum standards, i.e. countering harmful tax practices, preventing treaty abuse, introducing country-by-country reporting and improving the cross-border dispute resolution mechanism.[1]

In 2018, Hong Kong undertook a series of actions to meet the above criteria. In particular, under the transparency heading, Hong Kong signed the Multilateral Convention on Mutual Administrative Assistance in Tax Matters, which entered into force on 1 September 2018, to allow Hong Kong to effectively implement the AEOI and the BEPS package recommended by the OECD.[2] Hong Kong also codified transfer pricing rules and introduced documentation requirements.[3]

In terms of fair taxation, Hong Kong reviewed and amended its preferential tax regimes (i.e. the corporate treasury centre, professional reinsurance, captive insurance and offshore funds regimes) to ensure that they do not constitute harmful tax practices. "Ring-fencing" features were removed by extending the tax concession from non-domestic transactions to domestic transactions and introducing substantial activities requirements.[4]

Following these efforts, Hong Kong has been removed from the EU watchlist.

Comments

We welcome the decision of the EU to remove Hong Kong from its watchlist on tax cooperation in recognition of the efforts made by Hong Kong on the international tax cooperation front.

Hong Kong has demonstrated its commitment to meet the international tax standard by complying with good governance tax standards, addressing deficiencies in its tax system and combating cross-border tax evasion. This is essential for Hong Kong to preserve its competitiveness and reputation as an international financial and business centre, and to avoid being listed as a non-cooperative tax jurisdiction.

However, these changes made by Hong Kong will increase the tax compliance burdens of enterprises. Affected taxpayers should seek professional advice to ensure that they are in compliance with Hong Kong’s new rules.

[1] *For details, see our Tax Newsflash (Issues 59) published on 1 August 2017.*

[2] *For details, see our Tax Newsflash (Issues 57) and Tax Newsflash (Issue 63) published on 13 June 2017 and 19 October 2017, respectively.*

[3] *For details, see our Tax Analysis (H83/2018) published on 13 July 2018.*

[4] *For details, see our Tax Analysis (H86/2018), Tax Newsflash (Issues 82) and Tax Newsflash (Issues 91) published on 7 May 2018, 3 October 2018, 8 November 2018 and 13 March 2019, respectively.*

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